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UNCLAS SECTION 01 OF 04 SHANGHAI 000178

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STATE FOR EAP/CM, EAP/J, EB AND E  
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COMMERCE FOR ITA DAS KASOFF, MELCHER AND MCQUEEN  
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SUBJECT: JAPAN-CHINA RELATIONS BACK ON TRACK IN SHANGHAI

REF: 05 SHANGHAI 932

¶1. (SBU) Summary. According to Japanese contacts in Shanghai, Japanese Prime Minister Abe's October 2006 breakthrough visit to Beijing has dramatically improved the climate for Japanese investment in Shanghai, as well as led to an overall increase in cultural exchanges. The number of Japanese Chamber of Commerce members and travel between the two countries hit record highs in ¶2006. While new Japanese investment in China has slowed, contacts said this was natural as "those who should be here are already here" and some firms had begun considering moving operations to less expensive areas such as Vietnam. Though anti-Japanese sentiment among Chinese youth remained a concern, recent internet postings appear to be less virulent than in the past. Contacts noted that a lot was riding on Premier Wen Jiabao's April trip to Japan and speculated both sides would likely try to downplay any public differences until after the trip. End summary.

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"Those Who Should Be Here Are Already Here"  
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¶2. (SBU) Pol/Econ Chief and Econoff met with Bank of Tokyo-Mitsubishi UFJ's Shanghai Branch General Manager and former head of the Shanghai Japan Chamber of Commerce Makoto Motooka on March 16 to discuss the current economic climate for Japanese businesses in Shanghai. Motooka provided a positive assessment of the environment in Shanghai and noted that the number of Chamber members was at an all-time high of approximately 2000. Recent figures from the Chamber indicated that there were between 6,000 and 7,000 Japanese-owned businesses in Shanghai, including approximately 1,000-2,000 very small-scale enterprises.

¶3. (SBU) Motooka noted that new Japanese investment in China was down in both numbers of projects and total value and the rate of

growth in the number of Chamber members had slowed to just 10 percent in 2006, after 25 percent increases in both 2004 and 2005. He was not concerned by this slowdown and said it was natural since the initial wave of investment had ended and "those who should be here are already here." He added that although some speculated that the April 2005 anti-Japanese demonstrations in Shanghai and other cities in East China (see reftel) played a role in this slowed growth, their long-term impact had not been very significant.

14. (SBU) Contacts from the Japanese Consulate in Shanghai in a series of meetings in mid-March shared the same view as Motooka and reported that a "reassessment" of Japanese investment in China had begun even before the demonstrations. The rising costs of operating in coastal areas, especially salaries, and exchange rate fluctuations over the past three to five years had led many Japanese firms in East China to consider moving operations to lower cost regions in Southeast Asia such as Vietnam. Increasing concerns about the political situation after the demonstrations coincided with this economic reassessment, but should not be seen as the direct cause of the slowing growth of new investment.

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Increasing Disposable Incomes Benefit Japanese Companies  
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15. (SBU) According to Motooka, short-lived calls for boycotts of Japanese products in 2005 have had no lasting impact, as Japanese brands were highly admired by Chinese for their superior quality, even those products made in China. Major Japanese retailers such as Isetan, Sogo, Sanrio, Uniqlo and Muji remained extremely popular in increasingly fashion-conscious Shanghai. During the initial phase of Japanese investment in China, the focus was on building assembly capability in China

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for export to overseas markets. Most current investment projects, however, were now aimed at increasing or improving production capability intended for domestic Chinese markets. With the rapid rise in the number of Chinese with annual incomes approaching USD 10,000, consumers were becoming much more sophisticated and demanding. Just as in Japan 35 years ago, increased disposable incomes had changed behavior, with more consumers willing to pay more for "intangibles" such as quality, style and ease of use - traditional strengths of Japanese manufacturers.

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Abe's Visit to China "Dramatically" Changed Climate  
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16. (SBU) According to Motooka and Japanese Consulate contacts, Prime Minister Abe's breakthrough October 2006 visit to Beijing had "dramatically" changed the climate for major Japanese investment. Motooka cited the example of the international consortia bidding to construct the Shanghai-Beijing high-speed rail system. Motooka opined that in this new environment, "Japan can be selected."

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Second Largest Expat Community in Shanghai  
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17. (SBU) According to a Japanese Consulate contact, there were currently 45,000 long-term Japanese residents in Shanghai. Though the rate of new growth was slowing, Japanese still constituted the second largest expatriate community in Shanghai after Taiwan. [Note: There are approximately 20,000 long-term AmCit residents in the Shanghai consular district. End note.] Informal discussions with several private sector contacts and their families confirm that life in Shanghai remains very comfortable, with most enjoying the creature comforts which their similar position in Japan could not provide. None of our contacts expressed any concerns of personal safety or had directly experienced anti-Japanese sentiment in either their

daily lives or travels in China.

18. (SBU) Motooka noted that the number of Japanese employees assigned to work in China had been leveling off recently, although overall numbers remained strong. He added that with dramatic improvements in the quality of life in China's most cosmopolitan cities, Japanese employees were willing to take assignments in Shanghai or even Beijing. Recruiting staff to work in China's smaller cities, however, remained a major challenge. According to Motooka, with such a large presence, corporate social responsibility was becoming increasingly important to the entire Japanese community. The Japan Chamber of Commerce had recently built two schools in Anhui Province, provided financial assistance to 100 local students and donated 500,000 RMB to the Special Olympics ahead of the September 2007 Games in Shanghai. The Bank of Tokyo-Mitsubishi UFJ similarly provided 200,000 RMB per year to underwrite a series of 15 lectures on financial issues in the Masters of Public Policy program at Fudan University.

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Inbound and Outbound Tourism Hits Record Highs in 2006  
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19. (SBU) After a brief but significant drop-off in the number of Japanese visitors to China in the months following the April 2005 demonstrations, the situation has dramatically improved. The Japan National Tourist Organization reported that a record 3.745 million Japanese visited China in 2006 (vs. 3.334 million in 2004). According to Motooka, due to the geographic proximity and shared cultural affinity, many Japanese travelers still considered China to be an attractive destination. Chinese

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visitors to Japan in 2006 increased 24 percent to 811,700 (vs. 616,000 in 2004), also an all-time. Japanese Consulate contacts reported that growth in travel from Shanghai was particularly robust, as the Consulate issued more than 100,000 visitor visas to Chinese travelers in 2006, 25 percent more than in 2004. Consulate contacts also indicated that the thaw in relations since PM Abe's Beijing visit has resulted in a similar deluge of GOJ officials, often accompanied by business delegations, coming to China to meet their counterparts and survey the situation on the ground for themselves.

110. (SBU) One Japanese Consulate contact noted that to facilitate the rapidly growing number of travelers, establishing shuttle service between Tokyo's in-town Haneda Airport and Shanghai's Hongqiao Airport remained an important priority for both countries - and a key potential deliverable for future high-level meetings. [Note: Currently, all China-bound flights from Tokyo depart from Narita Airport, approximately 70 km from central Tokyo and all Japan-bound flights from Shanghai depart from Pudong Airport, approximately 30 km from the city center. End note.]

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Increasing Exchanges  
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111. (SBU) The serious interest in Japan and Japanese culture can be seen in the increasing number of Chinese students studying Japanese. According to Motooka, a record 210,000 Chinese students took the Japanese Proficiency Exam for Foreigners last year, 15 percent more than in 2005. Although anti-Japanese sentiment among young Chinese continued to be a concern, speaking Japanese was still a highly marketable skill, especially in Shanghai. Similarly, the number of students in Japan studying Chinese was also on the rise and interest in China was growing. As Motooka noted quite simply, "It pays!"

112. (SBU) On the cultural front, the situation in Shanghai has dramatically improved since PM Abe's visit to Beijing. Chinese event organizers now felt comfortable using the phrase "China-Japan" instead of "international." In fact, the press statement following Abe's visit announced that 2007 had been

named the "Japan-China Year of Culture and Sports," in commemoration of the 35th anniversary of the normalization of bilateral relations. The campaign, complete with an eye-catching logo (the "dynamic heart") and Japanese and Chinese catchphrases ("Carry the Hope Forward" in Japanese and "Hopeful Heart, New Future" in Chinese), is designed to "actively develop youth exchange" and "enhance friendly sentiment." When asked what events were planned for Shanghai, however, contacts from the Japanese Consulate were hard pressed to cite anything other than the (previously scheduled) series of Asian Football Championship matches in April and some associated soccer clinics for local children.

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Watch What You Say  
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¶13. (SBU) A contact from the Japanese Consulate said that recent postings on anti-Japanese websites and chat rooms appeared to be "less virulent" than in the past, with most netizens seemingly in line with Beijing's current engagement posture towards Japan. However, Japanese officials were still cautious in what they said. The contact stated that if a Japanese Finance Minister were to make public reference to the "underdeveloped" nature of the Chinese economy in the way that Secretary Paulson did during his recent trip to Shanghai, "there

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would be riots in the streets."

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Nanjing Massacre Anniversary Should Not Disrupt Relations  
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¶14. (SBU) Despite the upcoming the 70th anniversary of the Nanjing Massacre in December and the slew of Chinese, Japanese and even American films timed to coincide with the event, contacts said the commemoration was not a major concern and would not seriously affect the current state of generally positive relations between the two countries.

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Expectations For Wen's Trip  
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¶15. (SBU) While interlocutors were optimistic about Japan-China relations, many indicated that there was much riding on the success of Premier Wen Jiabao's April trip to Japan. Many anticipated that a successful outcome of the Wen visit could lay the groundwork for a visit to Japan by President Hu later this year. They said that in the meantime, there would be no significant changes to the status quo, and both sides would likely try to downplay any public differences which may arise before then.

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